Drafting and Interpreting Sensitive Gas Purchase Contract Provisions

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DRAFTING AND INTERPRETING
SENSITIVE GAS PURCHASE
CONTRACT PROVISIONS

by

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for the

NATURAL GAS SYMPOSIUM: CONTRACT
SOLUTIONS FOR THE FUTURE
REGULATORY ENVIRONMENT

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-G-
I. INTRODUCTION

A. Personal Bias

B. Gas Purchase Contract Characteristics

1. Contract/regulation confusion
2. Contract or option
3. Precision and ambiguity
   a. complexity
   b. weasel words

II. INDEFINITE PRICING

A. Escalators

1. Area rate clause
   a. FPC area rate
   b. any regulated price
2. Redetermination
   a. timing
      i. what triggers
      ii. notice required
      iii. frequency
   b. favored nations
      i. two or three party
ii. average prices

iii. other limitations

c. alternate fuel

i. specific fuel

ii. general reference

iii. transportation

d. market price

e. renegotiation

i. standard

ii. termination

f. arbitration

i. timing

ii. standard

B. Caps

1. Types

a. regulatory passthrough

i. gas

ii. "fraud or abuse" NGPA § 601(b)&(c)

A. new statute

B. intrastate purchaser

iii. facilities

iv. take or pay

b. marketability

i. standard

ii. discretion
c. competing fuel
   i. specific fuel
   ii. general reference

2. Operation
   a. prospective or retroactive
   b. automatic or optional
   c. cancellation mechanics
      i. buyer if refused by seller
      ii. seller if claimed by buyer
   d. notice mechanics

III. TAKE OR PAY

A. Objectives
   1. Producer
      a. cash flow
      b. present value
   2. Pipeline
      a. commitment
      b. flexibility
      c. ambiguity

B. TERMS
   1. General - agree to take, a minimum quantity, or pay for the part not taken
   2. Obligation Basis
      a. deliverability
         i. determination
            A. testing
            B. calculation
C. pressure
D. unrestricted flow
E. notice mechanics
F. arbitration
i. preconnection
A. determination
B. arbitrary standard

b. reserves
i. determination
ii. ratio
c. agreed amount
d. ceiling

3. Commencement
a. fixed date
b. connection
c. first delivery
d. agreement on basis
e. indefinite extensions
i. certificates
ii. force majeure
iii. indefinite obligation

4. Calculation Period

5. Pricing
a. Gas
i. end of period
ii. weighted average
iii. when not taken

b. Adjustments
i. taxes
ii. Btu

C. Makeup
1. Credit calculation
   a. gas or money
   b. price changes
2. Time limit
   a. fixed
   b. term of contract
   c. term extension
   d. early termination
      i. contract
      ii. single well
3. Cash payback
   a. general requirement
   b. special circumstances

D. Special Provisions
1. Deliverability cap
2. Seller billing or demand
   a. records
   b. routine procedures
   c. risk
3. Requirement for agreement
4. Carry-forward
5. Force majeure

E. Enforcement
1. Payment
2. Cancellation

F. Regulation
1. Direct
   a. prepayments distinguished
   b. unrecovered advance
   c. NGA 5 year makeup requirement
2. Indirect
   a. FERC Statement of Policy - December 16, 1982
      i. 18 C.F.R. § 2.103
      ii. deny interstate pipelines cost pass-through for take or pay in excess of 75% of deliverability in contracts after December 23, 1982
   b. Columbia Gas Transmission Corporation rate case
      i. FERC docket nos. TA81-1-21-001 and TA81-2-21-001
      ii. ALJ denial of take or pay passthrough
3. Proposed Regulation
   a. Senate Resolution 515
      i. passed December 14, 11982 (90 to 3)
      ii. encourages FERC to review administrative actions to prevent gas
price increases, including modification of take or pay clauses

iii. encourages producers and pipelines to renegotiate to recognize changed conditions

b. Proposed legislation
c. FERC

IV. BUYER OUTS
A. Pricing
B. Disconnection
   1. right to cancel
   2. uneconomic connection
C. Regulation
   1. direct
   2. indirect
D. Force Majeure
   1. detailed performance
   2. basic performance
E. Brute Force